

Tennessee Education Lottery

Estimates for Net Lottery Proceeds and After-School Program Funding



Presented to: The State Funding Board

Presented by: Robert N. Currey, Fiscal Review Committee

Monday, December 14, 2009

Presentation Outline

- Point of Reference - FY08-09 Actuals
- Legislative Change
- Lottery Industry Change & Expectations
- Sales Trends by Game
- FY09-10 Estimates (Current Year)
- FY10-11 Estimates
- Out Years
- Questions & Discussion

FY08-09 Actuals

	TOTALS	GROWTH Over FY07-08
Total Net Revenue (TNR)	\$1,020,570,844	2.4%
Total Expenses (TE)	\$755,084,716	4.3%
Net Lottery Proceeds (NLP)	\$265,486,128	(2.5%)
After-School Funding	\$14,666,222	6.9%
Total State Proceeds	\$280,152,350	(2.1%)

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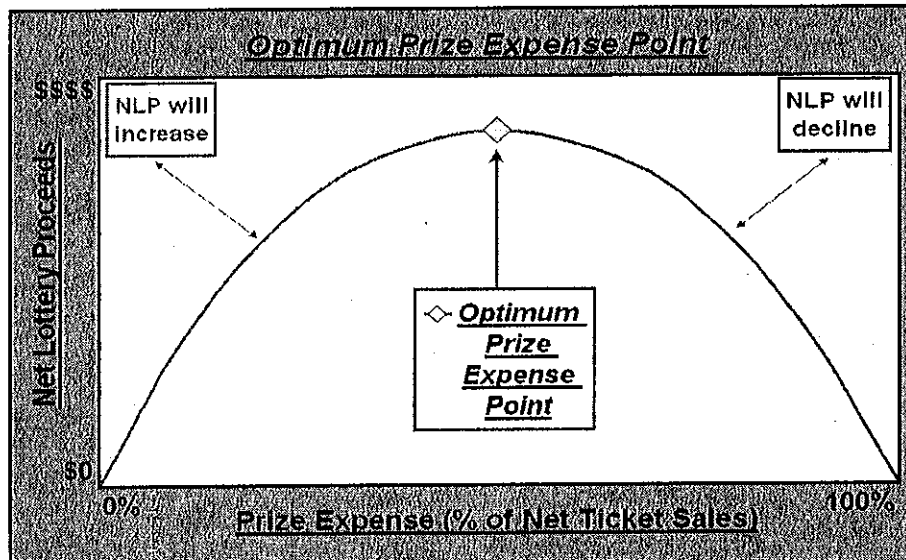
Why did NLP decline in FY08-09?

Year	Incremental Prize Expense	Incremental Expenses	Incremental Sales	Incremental Proceeds
FY05-06	\$89,715,982	\$103,002,284	\$145,441,347	\$42,439,063
FY06-07	\$51,574,745	\$55,478,759	\$57,584,975	\$2,106,216
FY07-08	\$5,052,645	\$5,102,434	\$5,549,510	\$447,076
FY08-09	\$31,044,242	\$30,926,747	\$23,997,308	(\$6,929,439)

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Profit Maximization



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Is TEL past the "Sweet Spot" now?

- Unknown
- If the economy rebounds (with improvements in employment, discretionary income, etc), and prize expense is held relatively constant, and Net Lottery Proceeds start to grow...
- Then, I would suggest (at a minimum) that the sweet spot is shifting towards the prize expense point being utilized by TELC.
- But, if economy rebounds, and prize expense continues to grow, and Net Lottery Proceeds continue to decline...
- Then, I am more inclined to say "yes".

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Each Dollar of Revenue

	FY03-04	FY04-05	FY05-06	FY06-07	FY07-08	FY08-09
Prize Expense	55.2%	57.9%	58.5%	60.3%	60.4%	62.1%
Retailer Commissions	7.1%	7.0%	7.0%	7.0%	7.0%	7.0%
Vendor Fees	2.3%	2.1%	2.1%	2.1%	2.1%	2.2%
Advertising	1.3%	1.9%	1.5%	1.3%	1.2%	1.0%
Other Gaming Expenses	0.4%	0.4%	0.4%	0.4%	0.5%	0.3%
Operating Expenses	2.5%	2.0%	1.7%	1.5%	1.5%	1.5%
Net Lottery Proceeds	31.4%	28.9%	28.9%	27.4%	27.3%	26.0%
Total Net Revenue	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

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FY09-10 (YTD)

- Through four months (October 31, 2009)
- Total Net Sales are up by 7.5%
- Incremental sales are \$23,507,053
- Total Expenses are up by 9.2%
- Incremental expenses are \$21,123,190
- Net Lottery Proceeds are up by 2.8%
- Incremental proceeds are \$2,383,863

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Legislation Change

Section 60, Public Chapter 531, Public Acts 2009 made a significant change to T.C.A. 4-51-111 regarding projections for net lottery proceeds

- In the past, the State Funding Board was required to project net lottery proceeds for the current and subsequent fiscal years
- PC 531 requires the State Funding Board to project net lottery proceeds for the current fiscal year and four subsequent fiscal years
- FY09-10 through FY13-14

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Lottery Industry Change

- There are two mega-jackpot lottery games:
 1. Powerball (PB)
 2. Mega Millions (MM).
- Lotteries can sell one or the other, not both
- 12 jurisdictions sell MM
- 33 jurisdictions sell PB (includes Washington D.C. and Virgin Islands)
- Jurisdictions with lotteries will have the option to cross-sell tickets for both games in early 2010

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Expectations

- Significant impact on the TEL
- Expected to generate incremental revenue and proceeds for scholarships
- Exactly how much more is unknown and very difficult to forecast

Lottery Industry Change

(CONTINUED)

Why is net impact so difficult to forecast?

- No sales history
- PB sales are expected to be cannibalized as players shift some purchases to MM
- As other states begin selling PB tickets:
 1. The population base of PB players will increase
 2. Cause PB jackpots to grow faster

Lottery Industry Change

(CONTINUED)

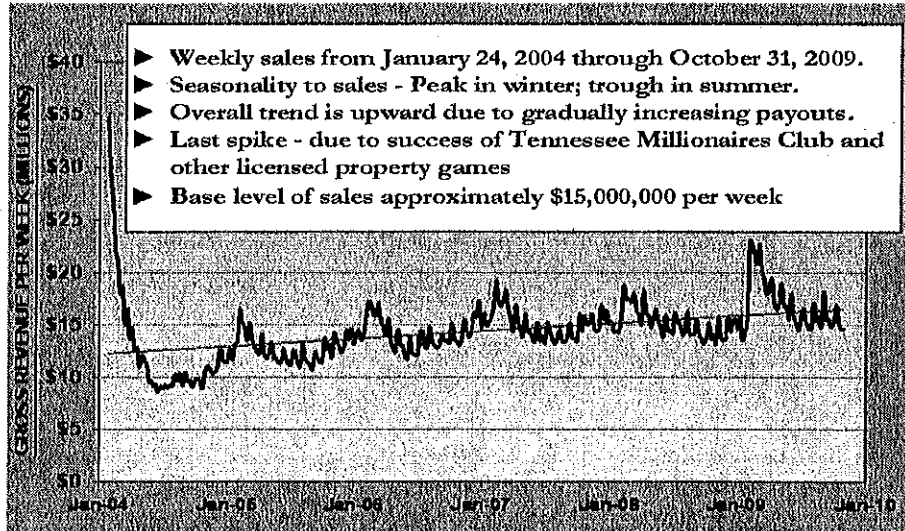
- Once MM tickets are sold, TEL will have drawings for two mega jackpot games four times per week
- PB drawings occur Wednesday and Saturday
- MM drawings occur Tuesday and Friday

Lottery Industry Change

(CONTINUED)

- TELC plans to discontinue Lotto Plus (LP) due to similarities with MM and PB
- Pick 5 sales are expected to increase as a result
- When LP was introduced in March 2008 it cannibalized sales of Pick 5
- The expectation is that some LP sales will shift back to Pick 5

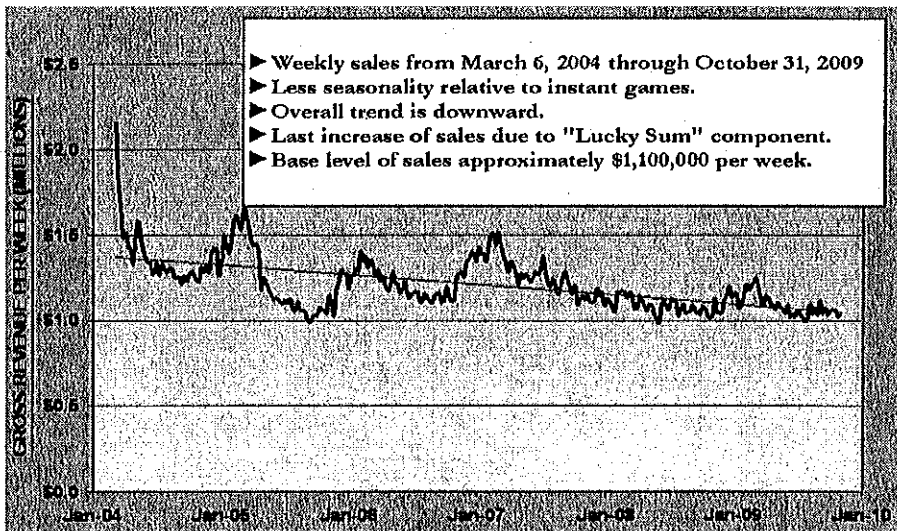
Instant Games - Since Inception



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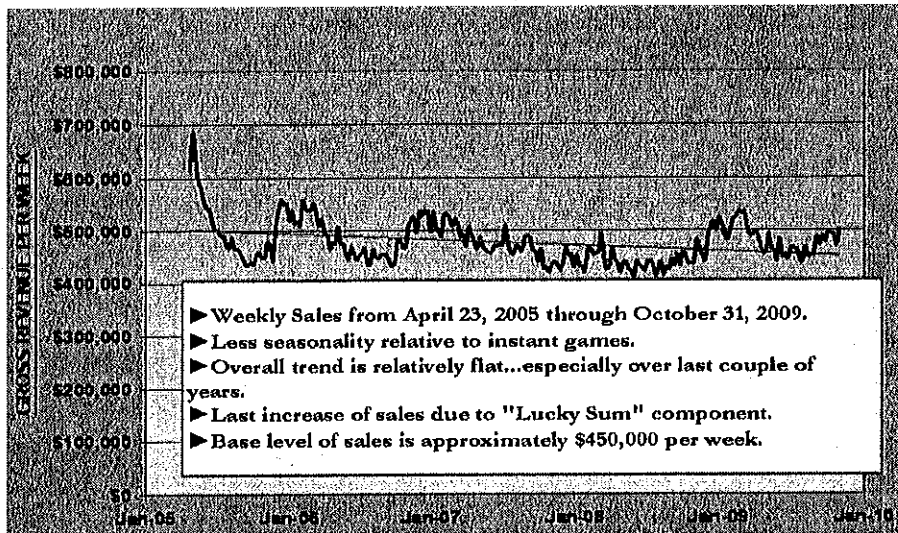
Cash 3 - Since Inception



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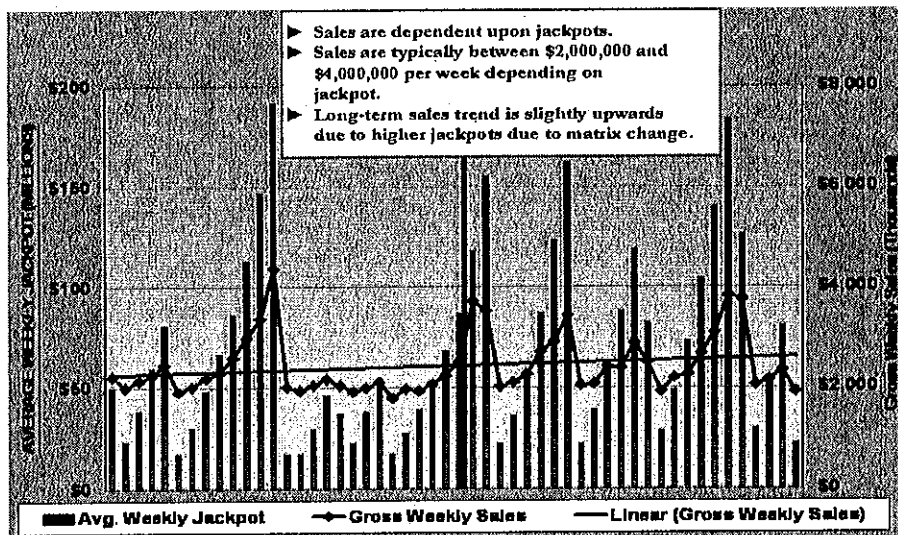
Cash 4 - Since Inception



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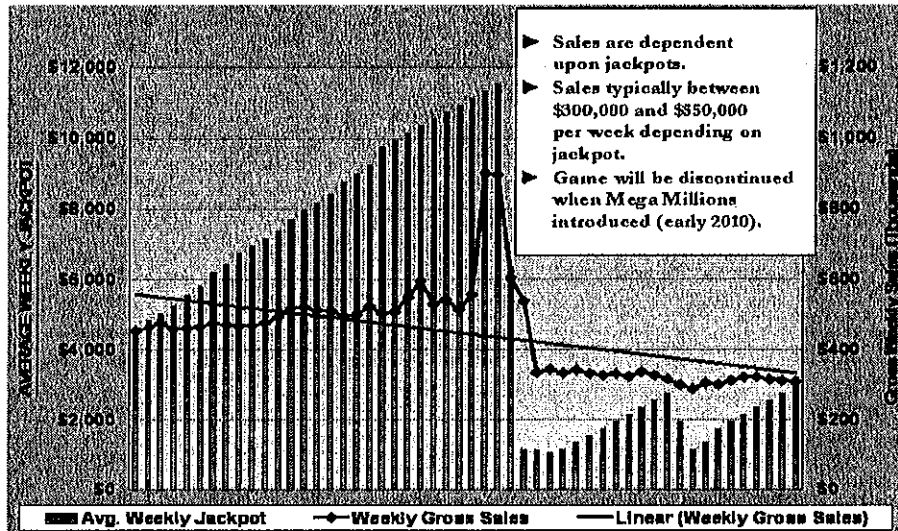
Powerball - Sales vs. Jackpots FY08-09



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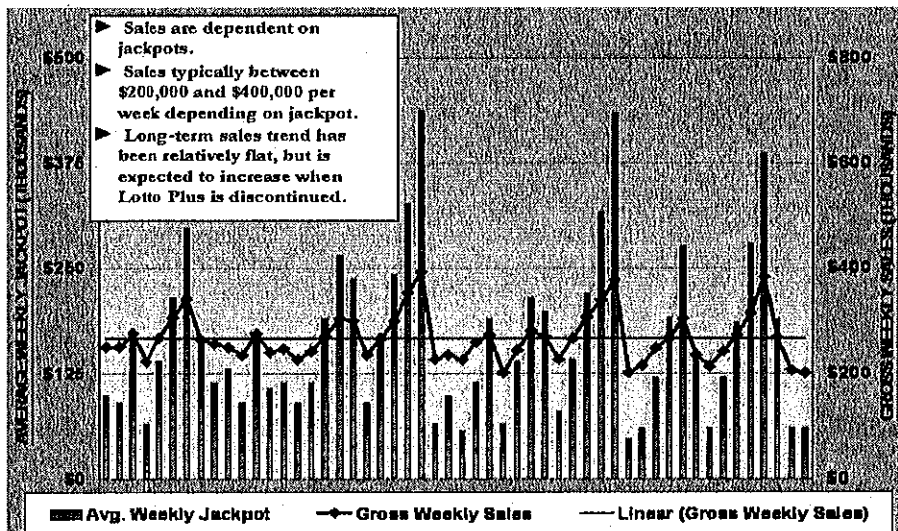
Lotto Plus - Sales to Jackpots FY08-09



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Pick 5 - Sales to Jackpots FY08-09



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Assumptions for FY09-10

- One new “spotlight” instant game.
- Prize payout ratio for instant games increase from 66.1% to 67.0%
- Instant game growth of approximately 2.0%
- Continued negative growth for C3 and C4
- Net sales growth for mega-jackpot games of approximately 18.4%
- No matrix changes for PB, MM, or Pick 5
- Total Expenses = 74.2% of Total Net Revenue
- Net Lottery Proceeds = 25.8% of Total Net Revenue

FY09-10 - Mean Estimates (1)

	TOTALS	GROWTH Over FY08-09
Total Net Revenue (TNR)	\$1,039,200,000	1.8%
Total Expenses (TE)	\$771,086,000	2.1%
Net Lottery Proceeds (NLP)	\$268,114,000	1.0%
After-School Funding	\$13,250,000	(-9.7%)
Total State Proceeds	\$281,364,000	0.4%

FY09-10 - Estimates (2)

Revenue Source	Low	Mean	High
Instant Games (Net)	\$774,000,000	\$784,000,000	\$794,000,000
Cash 3 & Cash 4	\$74,000,000	\$75,000,000	\$76,000,000
Pick 5 & Lotto Plus	\$24,000,000	\$25,000,000	\$26,000,000
Powerball & Mega Millions	\$140,000,000	\$150,000,000	\$160,000,000
Misc. Revenue	\$5,000,000	\$5,200,000	\$5,400,000
Total Revenue	\$1,017,000,000	\$1,039,200,000	\$1,061,400,000
Total Expenses (74.2%)	\$754,614,000	\$771,086,000	\$787,559,000
NET LOTTERY PROCEEDS (25.8%)	\$262,386,000	\$268,114,000	\$273,841,000
After-School Proceeds	\$12,500,000	\$13,250,000	\$14,000,000
TOTAL STATE PROCEEDS	\$274,886,000	\$281,364,000	\$287,841,000

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Assumptions for FY10-11

- Prize payout ratio for instant games increase from 67.0% to 68.0%
- Instant game growth of approximately 1.5%
- Slight negative growth for Cash 3 and Cash 4
- Net sales growth for mega-jackpot games of approximately 4.7%
- No matrix changes for PB, MM, or Pick 5
- Total Expenses = 74.4% of Total Net Revenue
- Net Lottery Proceeds = 25.6% of Total Net Revenue

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FY10-11 - Mean Estimates (1)

	TOTALS	GROWTH Over FY09-10
Total Net Revenue (TNR)	\$1,052,160,000	1.2%
Total Expenses (TE)	\$782,810,000	1.5%
Net Lottery Proceeds (NLP)	\$269,350,000	0.5%
After-School Funding	\$13,500,000	1.9%
Total State Proceeds	282,850,000	0.5%

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FY10-11 - Estimates (2)

Revenue Source	Low	Mean	High
Instant Games (Net)	\$791,840,000	\$795,760,000	\$799,680,000
Cash 3 & Cash 4	\$73,500,000	\$74,500,000	\$75,500,000
Pick 5	\$18,000,000	\$19,000,000	\$20,000,000
Powerball & Mega Millions	\$150,000,000	\$157,500,000	\$165,000,000
Misc. Revenue	\$5,200,000	\$5,400,000	\$5,600,000
Total Revenue	\$1,038,540,000	\$1,052,160,000	\$1,065,780,000
Total Expenses (74.4%)	\$772,670,000	\$782,810,000	\$792,940,000
NET LOTTERY PROCEEDS (25.8%)	\$265,870,000	\$269,350,000	\$272,840,000
After-School Proceeds	\$13,000,000	\$13,500,000	\$14,000,000
TOTAL STATE PROCEEDS	\$278,870,000	\$282,850,000	\$286,840,000

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Out Years

FY11-12, FY12-13 and FY13-14

- Sales growth is difficult to forecast due to the possibility of the following:
 1. Changes to payout ratios
 2. Matrix changes to jackpot based games
 3. Structure changes to other online games
 4. Introduction of new instant games, online games, and advertising, etc.

Out Years

(CONTINUED)

- Further complicated by the introduction of Mega Millions to TN because there is no sales data to reference where MM and PB have been cross-sold.
- Due to high level of uncertainty, projections for net lottery proceeds and after-school funding for the three out years remain fixed at FY10-11 levels.

QUESTIONS?



COMMENTS?